CallNet

CALL-NET ENTERPRISES INC.

ANNUAL REPORT 1996

Looking Forward to Our Second Decade

HIGHLIGHTS OF THE PAST DECADE

Annual Revenues *($ millions)*

1987	1988	1989	1990
• Call-Net provides enhanced services in Ontario & Quebec	• Federal Cabinet prevents telcos from closing Call-Net	• Call-Net initiates service in B.C.	• CRTC permits simple resale of private lines
• Call-Net develops first detailed billing program			

CONTENTS

1991

- Call-Net under new executive leadership
- Call-Net installs first Northern Telecom DMS-250 switch

1992

- CRTC landmark decision initiates full competition in long distance
- Call-Net founds Microcell
- Call-Net makes $30 million initial public share offering

1993

- Call-Net acquires Canadian rights to Sprint brand, technology
- Operating company renamed Sprint Canada
- Sprint Canada launches service in Alberta
- Call-Net acquires Cable & Wireless and Tell Canada
- Two Call-Net equity offerings raise $120 million

1994

- Availability of equal access to public telephone system permitting full competition
- Sprint Canada launches residential service
- Sprint Canada enters Atlantic Canada through Airway acquisition
- Call-Net acquires Insinc network management company
- Call-Net raises US $190 million in Senior Discount Notes

1995

- Sprint Canada completes fibre build in Central Canada
- Sprint Canada acquires STN assets
- Sprint Canada enters Manitoba
- Call-Net raises $108 million in equity

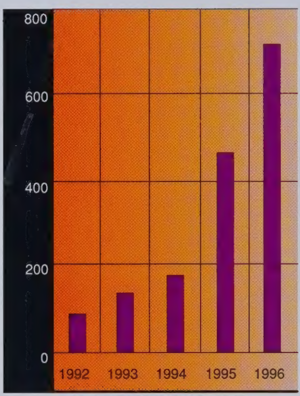
1996

- Sprint Canada augments network with fibre swaps
- Call-Net participates in CRTC local competition proceedings
- Sprint Canada enters Saskatchewan to complete national coverage
- Sprint Canada becomes #1 long distance alternative to telcos
- Microcell launches Canada's first PCS service
- Call-Net reports two quarters of net income

1991 1992 1993 1994 1995 1996

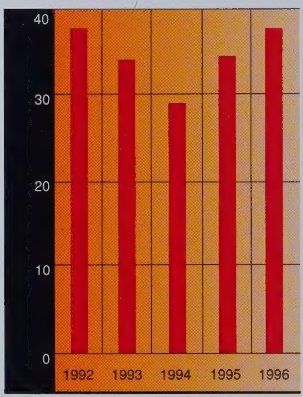
FINANCIAL HIGHLIGHTS

Revenue *($ millions)*



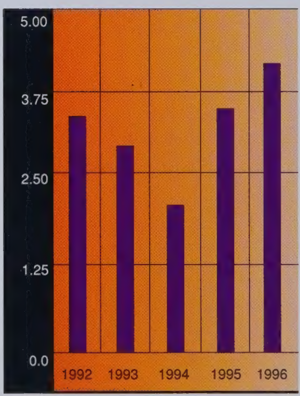
During the past five years, revenue has multiplied nearly nine-fold in response to regulatory changes that encouraged long distance competition. It reached $712.6 million in 1996, a 56% gain over 1995.

Gross margin *(% of revenue)*



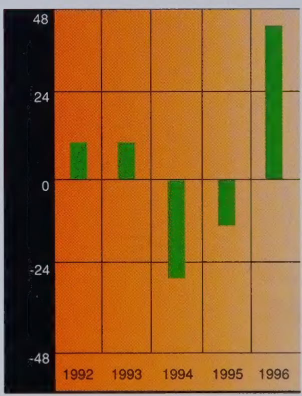
Carrier charges rose at a slower rate than revenue to produce a $267.9 million gross profit, a 72% gain over $155.5 million in 1995. As a percentage of revenue, gross margin improved for the third consecutive year to 38%.

Revenue / Capital assets



Although revenue expanded by 56% in 1996, capital assets rose by only 29%. Every $100 of capital assets supported revenue of $420 in 1996, compared with $347 in 1995 and $207 in 1994.

EBITDA *($ millions)*



After major investments to enter new markets in 1994 and 1995, we showed significant growth in 1996. EBITDA improved by $58.8 million from a $15.7 million deficiency in 1995 to a positive $43.1 million in 1996.

CORPORATE PROFILE

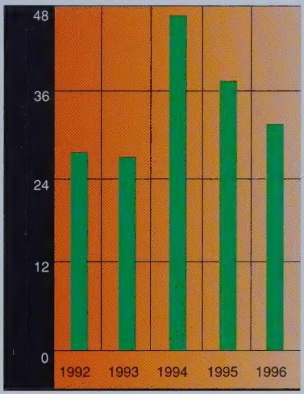
Call-Net's wholly-owned subsidiary, Sprint Canada Inc., provides long distance voice, data and network management services to consumers, businesses and governments across Canada. It is the nation's number one long distance alternative to the telephone companies.

Call-Net owns 19 percent of Microcell Telecommunications Inc., which is building a national digital wireless telecommunications PCS service.

Depending on regulatory decisions, Call-Net plans to offer local, mobile wireless and on-line communication services in 1997 and 1998.

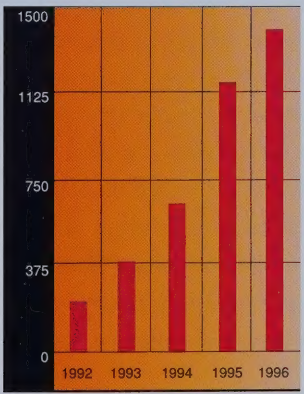
($ millions)	1996	1995
Revenue	$712.6	$457.5
Gross profit	267.9	155.5
Gross margin	37.6%	34.0%
EBITDA	43.1	(15.7)
Net loss	(7.1)	(64.7)
Cash flow from operations	51.5	(6.3)
Cash and short-term investments	170.1	179.6
Capital assets	169.7	132.0
Long-term debt	188.3	168.1
Shareholders' equity	253.0	249.5

Operating costs *(% of revenue)*



Our expansion strategy resulted in operating costs reaching 46.7% of revenue in 1994 before declining to 37.4% in 1995 and 31.5% in 1996.

Number of employees



Despite rapid staff expansion to 1,400 employees in 1996, productivity has continuously improved. Revenue per employee was $550,000 in 1996, compared with $500,000 in 1995.

CHAIRMAN'S MESSAGE

(Left to right) Chairman Juri Koor, Chief Counsel Robert Boron and Director of External Relations Wendy Iwai.

Call-Net Enterprises enters its second decade with a solid business foundation and a clear vision of the opportunities we can pursue.

Our long distance business has exceeded expectations. Since the arrival of widespread competition in mid-1994, Sprint Canada has emerged as the nation's largest long distance alternative to the telephone companies. During that time, our quarterly revenues have grown by 77 percent on a compounded annual basis. No Canadian telecommunications company has matched that rate of growth.

We have built this enterprise by focusing on doing a few things well and by arranging financing before every strategic move. We have maintained a conservative balance sheet, with a debt-to-equity ratio of 0.74:1, and our cash reserve of $170 million at the 1996 year end gives us the flexibility to make opportunistic new investments.

Profitability is building. Our EBITDA (earnings before interest, taxes, depreciation and amortization) performance tells the story. We invested heavily in building the long distance business in the second half of 1994 and throughout 1995. In every quarter of 1996, we achieved positive and rising EBITDA, culmi-

nating in modest net profits in each of the last two quarters. Our long distance services are projected to start generating free cash flow in 1997.

All this means that we are ready for our second decade and can continue to grow by leveraging our strengths. They include a reliable national network and modern network management resources; innovative billing systems that enable corporate customers to better manage their business; sales distribution channels across Canada; a large and growing customer base of households, companies and government; a low cost structure relative to long-established competitors; an enthusiastic and talented staff; and ample experience in managing fast-paced change in a very competitive marketplace.

In our second decade, we will solidify our position as Canada's most popular long distance company through growth in revenue and market share. By 2000, when Canadians are expected to spend more than $10 billion a year on long distance, we will be well on our way to a 15 percent market share, compared with just under nine percent at the end of 1996.

Second, within the next 12 to 18 months, we will enter the mobile wireless communications market by offering telephony and paging services bundled with long distance. Initially we will be a reseller, emulating our original entry into long distance. The wireless services market is expected to grow at a rate of 19 percent a year and by 2000 should be generating $5.6 billion in annual revenues.

Third, and starting in 1997, we will offer on-line and Internet services to consumers and businesses. Already, we provide Internet backbone access to many Internet service providers. The demand for on-line services is growing rapidly and the market should reach $2 billion in annual revenue by 2000.

Fourth, we expect to enter the local services market in mid-1998, utilizing a combination of leased and owned facilities, similar to the hybrid carrier strategy we pioneered in the long distance market. Canadian consumers and businesses are expected to spend $10 billion a year on local services by 2000. Our long distance customers have overwhelmingly endorsed us as their telecommunications provider of choice for local services.

This is an orderly strategy for growth that builds on the lessons learned in our first decade. One of those lessons is that competition gives Canadians real choice – and they want more choice based on the value equation of improved services and reduced costs. As competition spreads to other communications sectors, astute customers will quickly seek out the best value alternatives.

By the start of the next century, our expansion into mobile wireless, local and on-line services should transform Call-Net into a multi-billion dollar enterprise, with annual sales revenue more than triple the level of 1996.

We are also an investor in Microcell Telecommunications Inc. of Montreal, a company we founded in 1992. Our partners are well-known Canadian communications firms. Microcell is building a national digital wireless telephone service, called PCS (personal communications service). It will be about a year ahead of the other PCS licencee in establishing a market presence. We see considerable value accruing to our Microcell investment.

All in all, we are following a strategy of managed expansion. This, we believe, is the best way to ensure superior shareholder value. With our conservative balance sheet, cash on hand, and long distance services about to generate free cash flow, we are well positioned to finance our multi-service growth plan.

Over the next few years, we envisage a telecommunications world with less government regulation and greater competition. Further industry consolidation will occur, and globalization will impact Canada, reshaping the industry further through new alliances.

Our Company is well prepared for the opportunities and uncertainties that will arise as we strive to be Canada's communications company of choice.

Finally, we have taken special care to assemble a multi-talented executive team to carry our vision forward, supported by a board of directors with experience relevant to our strategic priorities. In that context, I want to express our profound thanks to Jim Dole and George Fuciu, both of whom retired recently as directors. Their knowledge and wise counsel will be missed. We welcome to the board Larry Tapp, Dean of the Richard Ivey School of Business at the University of Western Ontario, and Pat Smith, a technology executive at Sprint Corp.

Juri Koor

Juri Koor, *Chairman*

LONG DISTANCE SERVICES

Our long distance company, Sprint Canada, continues to grow at a record pace. We concluded 1996 with 820,000 residential long distance customers, clearly positioning us as Canada's largest alternative long distance company.

Our business list is also growing rapidly with more than 60,000 accounts by the end of 1996. New accounts signed up in 1996 included a growing number of large corporations. We are proud to provide service to distinguished organizations such as TD Bank, the Hudson's Bay Company, the Vancouver Stock Exchange, Medis Pharmaceuticals, the federal government's Human Resources Department, the Whistler Resort Association, GE Capital, Signature Vacations, and Arnold Brothers Transport.

These customers symbolize our future in the large user sector where we are still a relatively new competitor.

Our recent growth, with traffic volume rising to 2.8 billion billed minutes, compared with 1.7 billion minutes in 1995, confirms that Canadians see Sprint Canada as a communications company able to meet their needs, for now and for the future. We are proof that competition delivers tangible benefits to those seeking credible alternatives.

Sprint Canada is built on the philosophy of being market driven and customer focused. This philosophy pervades everything we do. And customers notice. Surveys confirm that our customers have higher satisfaction with Sprint Canada than Canadians generally do with the incumbent telephone companies.

We are delivering what Canadians want and deserve – a reliable national network, a wide choice of quality products and innovative services, proactive customer service around the clock, and substantial savings on their monthly bills, with guarantees.

For these reasons, we have become the first choice of Canadian households and business firms seeking an alternative to the telephone companies.

The Saskatchewan market opened to long distance competition for the first time in 1996. We now offer services in all 10 provinces.

Our recent success is also visible in our financial numbers. Revenue totaled $712.6 million in 1996 – a 56 percent increase over 1995. We made gains in every market segment and in every province.

We maintained a healthy gross margin at 38 percent of revenue as we continue to improve utilization of our large-capacity national network. This network ranks as one of the most modern in Canada. It consists of company-owned fibre optic circuits, leased transmission lines, major digital switching

Sprint Canada is a major Canadian corporation with employees in 17 offices across Canada. Leading the management team is Sprint Canada President and C.E.O. David Parkes (seated right) with (left to right) David Hagan, President of Consumer Services Group; Marion Code, Director of Human Resources; Ken Wilson, President of Business Services Group; and Doug Beatty, Vice President, Finance.

centres in Vancouver, Calgary, Toronto, and Montreal, a national data network and network management centres in Toronto and Vancouver. During 1996, we once again strengthened our network through fibre acquisitions and new construction. The company also has two 24-hour customer service centres, and 17 offices from coast to coast.

The growth in customers, traffic and revenues has forced Sprint Canada to mature as a company. Our payroll has been growing rapidly to the point that we now employ more than 1,400 Canadians. Despite this growth, we have remained highly efficient, with revenue per employee of about $550,000. This is a great tribute to the dedication and enthusiasm of our staff.

To ensure we adhere to the highest professional standards, and that our managers keep pace with customer demands and technological progress, we have developed a series of training seminars and personal development courses. These are built around our corporate values of *teamwork* in the company, *responsiveness* to customer needs, *innovation* in finding solutions that exceed customer expectations, and *balance* between work and family commitments. Now that we are a major corporation, we accept our responsibility to help our people be the best that they can be in every respect.

Our corporate maturity is also reflected in our first national sponsorship; we now provide time, talent and financial support to the Canadian Special Olympics across the country.

Looking ahead, we see an exciting future and will continue our commitment to growing the Company in all market segments.

In the residential area, our new THE MOST™ by the minute savings plan announced in February 1997 is already having an impact. It is the first of its kind in Canada and finally frees Canadians from a long history of rules and restrictions over the best times to make long distance calls to enjoy discounts. Our plan fundamentally changes long distance competition to the benefit of customers.

On the business side, we are making steady inroads among large corporations and governments, which have the technical resources to make astute telecommunications decisions.

We are also developing new products and services for consumers and businesses. We plan to offer Canadians competitive choices in paging and mobile telephone services bundled with our long distance services. We will also roll out a basic Internet dial up product for consumers, followed later by new Internet and intranet services for businesses.

THE BENEFITS OF COMPETITION

As the "Highlights of the Past Decade" tabulate at the beginning of this annual report, competition in Canadian long distance telecommunications has emerged in stages – in 1987 when Call-Net pioneered the resale of enhanced services, in 1990 when the CRTC permitted simple resale of private lines, in 1992 when the federal regulator approved WATS resale and facilities-based competition, and finally in 1994 with implementation of equal access to the public telephone system.

As a major telecommunications company and a strong advocate of competition, we wanted to document what long distance competition had achieved and how it has benefited Canada. To this end, Call-Net commissioned a study by the internationally recognized firm KPMG. It developed three perspectives:

(i) a benefit-cost analysis perspective, which measures the benefits of long distance competition to the Canadian economy as a whole by measuring the difference between the value of telecom services consumed by Canadians and the cost of producing those services;

(ii) the economic impact perspective, which describes how competition has affected employment, capital spending and inflation; and

(iii) the competitiveness perspective, which examines the effects of competition in long distance services on the competitiveness of Canadian businesses as users of telecommunications, and of the Canadian economy as a whole.

The study concluded that: "Competition in long distance services has created substantial benefits for Canadians and for the Canadian economy as a whole. It has encouraged strong growth in the use of telecommunications services, which has permitted employment in the industry to remain stable despite significant productivity increases brought about by competition."

The following are among the key findings of the KPMG study:

- Long distance competition delivers at least $5 billion more a year in benefits to Canadians than would have been the case without competition.
- Long distance rates are approximately 55% less than they would have been without competition.
- Long distance voice and data traffic volumes are 67% higher as a result of the pricing and service impacts of competition.
- Many of the industries that are heavy users of telecommunications services are in the growth sectors of the Canadian economy, and have benefited substantially from competition in long distance services. When industry sectors are ranked by growth rates in output and employment, the fastest growing sectors use telecommunications four to five times as intensively as the economy as a whole.
- Competition has spurred additional growth in productivity in the telecom sector. This additional growth is estimated at 1.8 percentage points per annum since 1986. The value of output per employee (after removing the effects of inflation) has more than doubled.
- Despite large increases in output, employment in the telecom industry was roughly the same in 1995 as in 1983 (about 114,000 employees). Significant productivity growth occurred without job loss.
- Over the last decade, capital expenditures in the telecom sector have been $2 billion higher than they otherwise would have been without competition. New entrants have significantly increased their share of total investment.

There is no question that the introduction of long distance competition has been one of the most valuable and economically efficient public policy decisions ever undertaken by Canada.

Call-Net is getting ready to compete in local services – the next major area of telecommunications expected to be opened to new entrants. Leading our efforts is (left) Phil Bates, President and C.E.O. of Call-Net's Local Services, assisted by (standing) Jean Brazeau, Vice President, Regulatory Affairs; and Bruce Hughes, Vice President of Marketing and Sales, Local Services

LOCAL SERVICES

We were a lonely irritant to the telephone companies in 1987 when we launched long distance competition by buying capacity at bulk rates and reselling it at a discount to business users. But our detailed billing service made sense to businesses trying to manage their telecommunications costs. Now, a decade later, long distance competition is an accepted fact among Canadians.

The next major competitive revolution will be in local services and Call-Net will be among the first to challenge the telephone companies in a market they have owned for more than 100 years. The CRTC is expected to set the terms and conditions of local competition by mid-1997. Assuming an acceptable decision, we hope to launch our first products in 1998 after completing market trials.

The local market is attractive for several reasons. One is its size. Business and governments spend $3.9 billion a year on voice and data services, consumers $3.4 billion on local telephone services, and long distance providers $700 million for local access to the public telephone system.

The local market is expected to grow at a compounded annual rate of 8.5 percent (compared with six to seven percent for the long distance market) to reach $10 billion in revenues by 2000. This growth will be driven by local rates being more closely aligned with costs and by increasing demand caused by innovative marketing and product development by new entrants.

Our success in long distance, driven by a commitment to customer service, product innovation and competitive pricing, combined with a proven hybrid carrier network strategy, gives us the confidence that we can be successful in the local market. Market research shows that many of our customers want to buy local services from us.

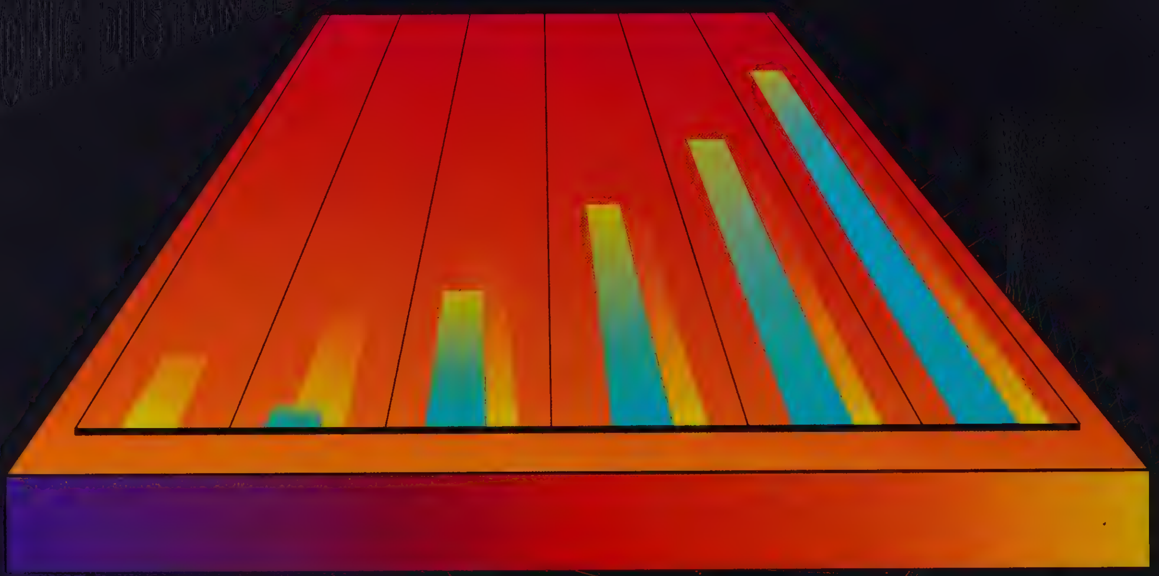
Compared with our entry into long distance a decade ago, we are in a strong position and can leverage such assets as our national network and network management services, a large and satisfied customer base, innovative billing systems, sales distribution channels, customer service call centres, and management competence in developing and launching new products on new platforms. A major advantage is that we are a relatively low cost operator and an efficient user of capital.

We will use a hybrid carrier network strategy in providing local services, employing a combination of owned and leased facilities, as well as resold local services. Depending on the CRTC's decision respecting local services competition, our plan will involve investing in our own facilities, particularly in urban markets, and reselling the telephone companies' local services in rural markets. We anticipate that over time, as our customer base grows, we will invest in our own facilities in progressively smaller markets.

We are dedicated to being a top competitor and will make the investments required to ensure Canadians receive the full benefits of local competition. Consistent with our history, we will follow a tightly managed approach by doing a few things well before broadening our strategy.

THE NEXT DECADE

LONG DISTANCE



CALL-NET'S EXECUTIVE MANAGEMENT

Philip Bates, *Senior Vice President, and President and Chief Executive Officer of Call-Net's Local Services Group.* Joined Call-Net as Vice President of Network Services in 1990. Served as President and Chief Operating Officer of a wireless access provider during 1995. Rejoined Call-Net in February 1996.

Robert Boron, *Senior Vice President, Chief Counsel and Secretary* since April 1996. Joined Call-Net in November 1990 as Legal Counsel. Previously worked at Revenue Canada and Johnston & Buchan in Ottawa, specializing in communications law.

Jim Hardy, *Vice President and Chief Financial Officer* since April 1996. Joined Call-Net in April 1992 and subsequently appointed Vice President of Corporate Development in 1995. Previously involved in communications and technology finance at a major Canadian financial institution.

David Parkes, *Senior Vice President, and President and Chief Executive Officer of Sprint Canada Inc.* Joined Call-Net in January 1995. Formerly a sales and marketing executive with a national mobile telephone service carrier, and held senior positions in the food service and retail industry.

David Hagan, President of Consumer Services Group, and staff check the strong consumer response to Sprint Canada's new flat rate program The Max™ by the minute savings plan.

THE CHOICE FOR CONSUMERS

Sprint Canada is the most popular choice among Canadian households seeking a long distance alternative to the telephone companies. We ended 1996 with 820,000 customers, an increase of more than 200,000 in one year. We offer service in all 10 provinces following the opening of Saskatchewan to competition in November 1996.

In February 1997, we introduced The Most™ by the minute savings plan offering a flat rate of 15 cents per minute for calls to anywhere in Canada at any time on any day and 22 cents per minute for calls from Canada to anywhere in the United States at any time on any day. Low by-the-minute rates apply to overseas calls. The plan provides the best long distance savings with no limits or restrictions.

Consumers still have the choice of our The Most™ 50% off savings plan, which delivers a 50 percent saving on every call to the three numbers talked to the most each month – one number within Canada, one number to the United States and one number overseas, plus a 15 percent discount on all other calls. Customers who call overseas less frequently automatically receive 50 percent off the second most talked to number in Canada. All savings are off the standard time-of-day rates charged by the telephone companies.

In 1996, we introduced the industry's first savings guarantee, offering double the difference if a customer could save more from the telephone company on their monthly invoice. Competitors have yet to match this initiative.

Our customers have told us that they want Sprint Canada to provide a broader array of communications services beyond long distance. Compared with the general population, Canadians who choose Sprint Canada tend to be high income, well educated, young, urban, international in their contacts and enthusiastic users of technology. They spend more on long distance services than the average household and are higher-than-average spenders on paging, mobile telephone and Internet services.

Our customers are also very loyal and it is remarkable that more than 70 percent have referred someone else to our service.

We expect to be among the first in North America to bundle long distance, local, wireless and on-line services as a single package. Our strategy for providing a single source and single billing for communications services reflects our philosophy as a market-driven and customer-focused company.

Sprint Canada

THE CHOICE FOR BUSINESS

Sprint Canada has been serving the telecommunications needs of Canadian businesses for more than 10 years.

We began by delivering cost savings and value-added services to small firms. Initially, we offered outbound voice services with detailed and consolidated billing reports. The small business market, where firms spend less than $1,000 a month on long distance, remains an important part of our customer base.

In recent years, we added inbound (toll free) and outbound voice and data services that are attractive to firms spending up to $20,000 a month on long distance. We have a high share of the medium user market, where our toll free, Fōncard™ telephone card, call detail reporting and bill analysis software products are in strong demand.

The reliability and global reach of our nationally-available service has particular appeal to large corporations and governments, which represent three-quarters of business spending on long distance. We offer voice and data services, including high-speed private line, global frame relay, router management, X.25 service, virtual private network, Internet backbone access and, since November 1996, teleconferencing. Most of all, we offer effective solutions to complex requirements.

1996 ended with more than 60,000 business accounts. Our revenue share of the business market exceeds seven percent and should more than double by the end of the decade.

In considering alternatives to the telephone companies, many large users are initially concerned about network reliability. Our proven network reliability is equal to or better than our competitors. We deploy SONET technology throughout our network to recognize a fibre break and reroute a call within 50 milliseconds – too short a time for a customer to even notice an interruption. We also provide high-quality SONET ring protected private lines at very competitive prices.

We employ the latest technology at our network management data centre in Vancouver and a similar network management voice centre in Toronto. Either centre can run the entire national network.

In terms of North American service, three transborder rings from Vancouver, Toronto and Montreal provide seamless voice and data service to the U.S.

A concern of prospective customers is whether a relatively young company has the breadth of expertise and long-term staying power to service their continuing needs. Customers are impressed by the knowledge and experience of our technical staff, as well as our commitment to after-sale customer care. Customer responsiveness is, in fact, one of Sprint Canada's four core values and has shaped our corporate culture. Furthermore, we have proven our financial viability in the past two years.

Finally, we strive to be cost competitive and provide the customer with a full cost-benefit analysis of our recommendations.

The large business market is becoming aware of the advantages that Sprint Canada can bring to their telecommunications services. As we expand our long distance customer base, we will add complementary communications services.

For example, the CRTC has completed hearings on whether long distance companies should have equal access to the national cellular telephone services and the new mobile wireless telephone networks. In the event of a positive decision, we will offer long distance options to mobile telephone users.

In the case of on-line commercial services, a third of Canadian companies will have an intranet before the end of 1997. We are developing a service that will position Sprint Canada's strengths in this area. We are already Canada's largest supplier of Internet backbone access, providing service to nearly half of the country's current 350 to 400 Internet service providers.

Ken Wilson, President of Business Services Group, and his regional vice presidents review the growing demand among major corporations for Sprint Canada's national voice, data and network management services.

"They're extremely proactive and made us the most confident."

Fred Taylor

Arnold Bros. Transport Ltd.

"Now we have an even better deal to share with [our] members."

Jim Watson

Whistler Resort Association

THE CHOICE OF MAJOR USERS

Our emergence in the corporate world is best told by our customers who scrutinize everything we do from network reliability to cost controls.

Sometimes persistence pays off. In Whistler, British Columbia, the 4,000 businesses and condominium owners in the valley are members of the **Whistler Resort Association**. For many years, the WRA managed a program that shared long distance discounts with members. When we persuaded several members to switch to Sprint Canada, the Association called us in for a chat and then decided to tender its toll free business. "Sprint Canada was the clear winner," explained Jim Watson, WRA's vice president of finance and administration. "Now we have an even better deal to share with members." He described Sprint Canada's North American toll free service as "unbelievably less expensive." Early in 1997, the WRA switched all of its long distance traffic to Sprint Canada.

Besides winning "virtually the whole town" as long distance customers, we also provide the WRA with dedicated toll free fax lines to Brazil, Mexico and Germany. As Jim Watson observed, this is a better solution than voice service for travel wholesalers and the Association because of the time differences. He also lauded Sprint Canada's software billing program, which makes it easy to allocate charges among members and analyze customer response by area code, time of day and other criteria so that the Association can fine-tune its marketing efforts.

From Winnipeg, **Arnold Bros. Transport Ltd**. runs one of North America's largest trucking operations. Continuous communications with its drivers and customers is critical – and expensive. The company began to hear from Sprint Canada as soon as we opened our office in Winnipeg. Eventually, Arnold Bros. decided the best thing to do was to put its voice services out to tender. Sprint Canada won, according to Fred Taylor, manager of information services, because of the clarity of the service, the network reliability, and the attentive customer service. "They're extremely proactive and made us the most confident," he noted.

Arnold Bros. was so impressed by their improved voice service that they assigned their data service to Sprint Canada in 1995.

We now provide frame relay service to the company's branches across Canada and the United States.

Two recent examples of our tenacity in winning contracts for complex data applications are the Alberta Stock Exchange and the Vancouver Stock Exchange.

In 1995, the **Alberta Stock Exchange** made the mission criti-

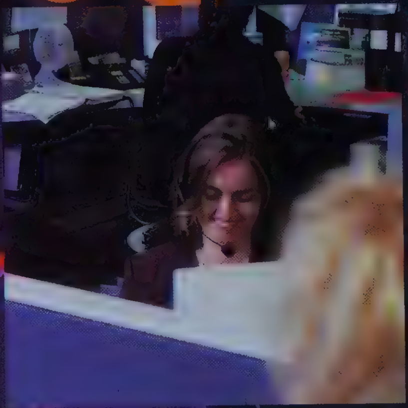
cal decision to close its trading floor and introduce an electronic trading network in 1996. It also decided to outsource network management to a supplier who could provide global network services and ongoing national network support – all at competitive costs. Sprint Canada met the criteria. "We felt that Sprint Canada understood the problem better than others and was more innovative. Because of that, they were cost effective," commented Jeff Meyer, ASE's director of information services. "They provide us with end-to-end management of the network. Being a national provider is very important. We needed a partner with global reach." He added that "Sprint Canada went the extra mile with something they stand behind."

Winning the ASE business was a valuable credential when the **Vancouver Stock Exchange** decided in 1996 to migrate from an X.25 service to newer technology for its computerized trading network. It asked for tenders. We proposed a frame relay solution, with ISDN backup, disaster recovery and multiple levels of redundancy.

"All suppliers could have chosen the same solution and presented the same network reliability," explained Marc Foreman, VSE vice president, trading and market information services. "Sprint Canada came forward with the reliability and the guarantee of reliability. They were willing to step up to the mark and get the job done and guarantee they'd get the job done."

Added VSE's vice president and chief financial officer Lloyd Costley, "We wanted an organization with a national network that had the depth of experience and expertise to appreciate the unique network requirements of the Exchange's state-of-the-art fully automated trading system. We also needed an organization that could deliver an effective network solution within aggressive timelines ... and which could work well with our trading and technology staff."

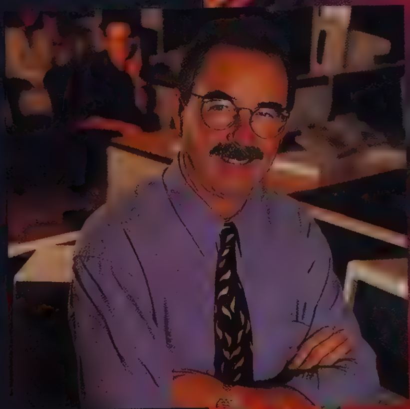
Network reliability was also a prerequisite for **Medis Health & Pharmaceuticals Inc**. of Montreal, considering the mission critical nature of its business – filling health product orders from pharmacies and hospitals across Canada. Since 1995, Sprint Canada has provided Medis and its national branch network with inbound and outbound long distance services. "We had two carriers and decided to aggregate our costs and achieve volume savings," remembered Domenic Silvaggio, Medis' office systems manager. After reviewing proposals from four suppliers, Medis selected Sprint Canada "because we wanted a national carrier who guaranteed reliable service. We can't afford to go down and we were impressed by the terms and costs they gave us." He added: "We even brought in a consultant and he told us 'you can't get a better deal than the one you've chosen.'"



"Sprint Canada offers a consistent level of reliable service."

David Livingston

TD Bank



"They deliver all the service features of our previous supplier, but at a lower price."

Mike Nieder

Hudson's Bay Company

Large corporations often take a cautious approach to contracting a new supplier. **TD Bank,** for example. After winning a tender call in 1995, we were selected to provide toll free service for TD's Visa operations on a one-year trial. Satisfied with the service, the Bank decided in mid-1996 to retain our toll free service for its telephone and on-line banking as well as its mutual fund organization. While cost is always a factor, David Livingston, TD's senior vice president of card and direct services, notes that "Sprint Canada offers a consistent level of reliable service. This is very important because network reliability is critical. If we don't have a reliable network, we don't have a business."

Canada's oldest retailer, the **Hudson's Bay Company**, also took the trial approach. Its coast-to-coast voice and data networks link more than 400 stores. It retained Sprint Canada for 12 months in 1995 to provide its customers with toll free access to Bay and Zellers call centres in Vancouver, Toronto and Montreal. Impressed by the service, it decided in 1996, after reviewing proposals from four suppliers, to switch all long distance traffic to Sprint Canada. We also provide high-speed Internet access to its recently introduced web site.

Part of the attraction is our call reporting service. Hudson's Bay allocates charges to its 400 stores in a couple of hours – compared with 16 hours previously. "We are delighted with the way Sprint Canada works with us," commented Mike Nieder, general manager of computing and communications. "They deliver all the service features of our previous supplier, but at a lower price." Hudson's Bay recently selected our teleconferencing service for electronic meetings of its district managers across Canada.

I-Fax International Limited, a global telecommunications enterprise based in Halifax, has a big appetite for voice and data services. "We handle huge volumes of traffic around the world," explained president Cris Worthington.

Today, I-Fax uses our toll free, outbound long distance, X.25 and frame relay services as well as direct digital data lines. "We are a heavy user of data service," Mr. Worthington explained. "Sprint Canada's association with Global One was very interesting to us. We depend on international toll free service so that when someone in a foreign country dials their local 800 service to send a fax, it comes directly to Halifax. We needed the cooperation of Sprint to get lines into many of these countries."

Based on his experience, he added: "If telecommunications is important to your enterprise, you need to do business with these guys."

CORPORATE GOVERNANCE PRACTICES

The Company's corporate governance practices are consistent with the guidelines of the Toronto and Montreal stock exchanges and the expectations of investors.

The board has assumed stewardship of the Company in overseeing the efficacy of senior management and ensuring that effective policies and procedures are in place to satisfy its fiduciary duties.

Call-Net does not have a controlling shareholder and the board and its committees are dominated by independent directors. The qualifications and affiliations of each director, as well as the mandate of each committee, are described on the next page.

Seven of the nine directors are considered to be unrelated – that is, they are free from any interest or relationship with Call-Net that could reasonably be perceived as materially interfering with their ability to act in the best interests of all shareholders. The unrelated directors include three executives of Sprint Communications Company L.P., which has a 25 percent non-voting economic interest in Call-Net.

An annual strategic planning process is in place and the directors are kept apprised of risks to the business and management's strategic response.

A comprehensive compensation-for-performance policy aligns the interests of management with those of the shareholders.

The board is proactive and meets often, specifically 15 times in 1996.

The directors acknowledged in last year's annual report that certain aspects of Call-Net's corporate governance needed to be addressed – director and management succession planning, the mandates and membership of board committees, a formalized process for evaluating board performance, the continued appropriateness of combining the functions of Chairman and Chief Executive Officer, and the diversity of board membership.

The board took major initiatives in 1996 to address these and other issues. First, it formed a corporate governance and nominating committee, chaired by a new outside director, Lawrence Tapp, Dean of the Richard Ivey School of Business at the University of Western Ontario. Second, it commissioned a study by the National Association of Corporate Directors (NACD) of Washington, D.C., to provide a full assessment of Call-Net's board and committee effectiveness, skill set, operations and corporate governance practices. Third, it established mandates for, and removed inside directors from, all committees.

The NACD study recognized that Call-Net is in transition from an entrepreneurial venture to a mature and ultimately "multi-billion dollar" public corporation. It observed that the board has dedicated and knowledgeable members. Recommendations were made on the need to select independent directors with core competencies and skills in telecommunications, large-company management, marketing and financial markets.

The study recommended improvements in board/management communication; an improved board and director evaluation process; a process for board member succession; and the need for CEO succession planning. The current combination of the CEO and Chairman functions is not considered a major concern in view of Call-Net's structure as a holding company with operating subsidiaries led by chief executives.

The corporate governance and nominating committee will act on the recommendations of the NACD study, as well as other initiatives, in 1997.

BOARD PROFILES

COMMITTEES

Audit: Reviews financial controls and risk management, reporting procedures, internal controls and the performance of the external auditors. Evaluates management's financial performance.

Compensation and Human Resources: Reviews executive and director compensation, including incentive-based compensation programs for management. Establishes measurable performance criteria. Responsible for the search and appointment of senior management.

Corporate Governance and Nominating: Establishes formal corporate governance guidelines and practices. Reviews credentials of board members and nominees. Recommends candidates for nomination. Sets guidelines for the education and orientation of new board members.

BOARD MEMBERS

Honourable Alan R. Abraham, C.M., C.D.: Former Lieutenant Governor of Nova Scotia. Former President and Chief Executive Officer of Maritime Warehousing & Transfer Co. Ltd., Halifax.

Robert Crockford: University of Western Ontario business graduate. President of Valley City Manufacturing Company, Dundas, Ontario since 1978. Founding director of Call-Net.

Juri Koor: University of Toronto industrial engineer. Held management positions in computer, manufacturing and financial services industries in Canada, Europe and United States. Joined Call-Net as President and C.E.O. in 1991, and subsequently became Chairman.

David Parkes: York University B.Sc. and MBA graduate. Held management positions in food services industry, president of a leading restaurant chain. Senior sales and marketing position at a national mobile telephone service carrier. Joined Sprint Canada as President and Chief Executive Officer in January 1995.

Patrick Smith: MSC from University of Manitoba. Director of computer centre and lecturer in computer science at University of Manitoba for 13 years. Joined SHL Systemhouse as Chief Technology Officer in 1983. Joined Sprint Corp. in 1995. Now Vice President, Systems Integration and Technology Planning.

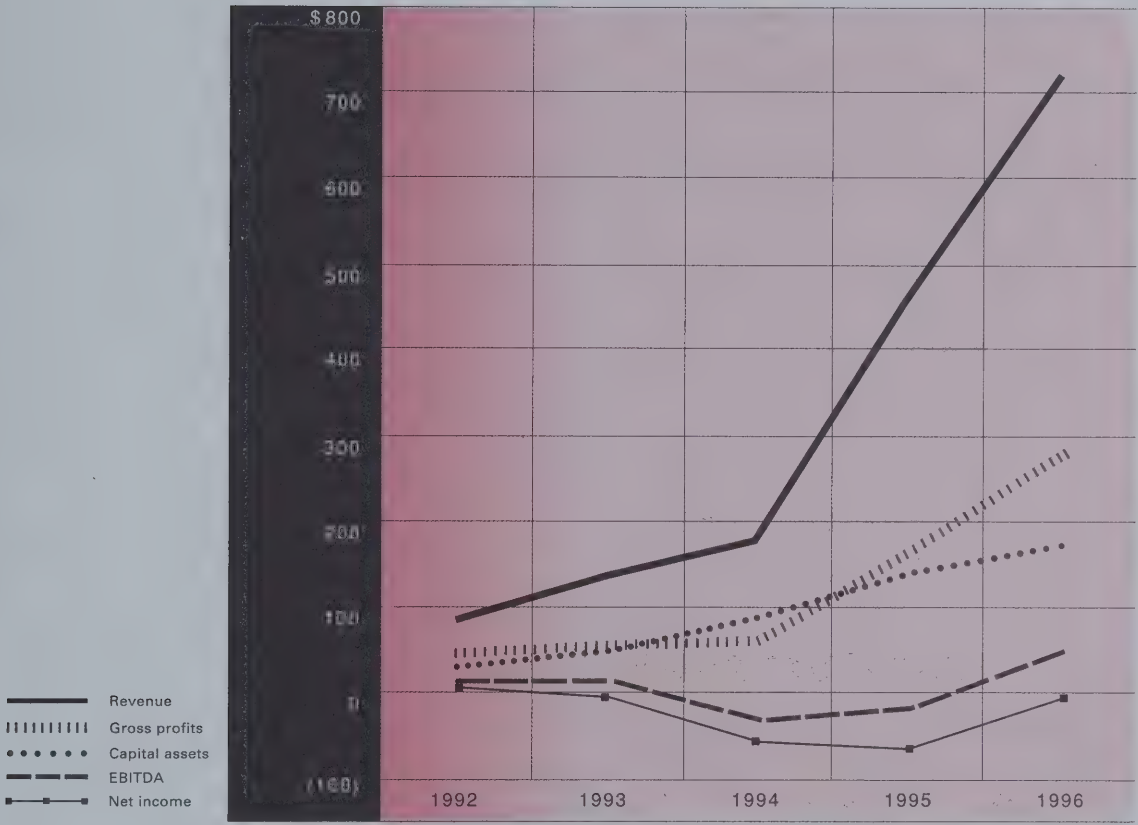
Lawrence G. Tapp: Dean of the Richard Ivey School of Business, University of Western Ontario. Long career in private sector. Served as President of the packaging company, Lawson Mardon Group, and led its leveraged buyout.

J. Herman Vanderlaag: University of Calgary electrical engineer. Long career in telecommunications. In 1983, formed Catcom Systems Corp., designer of voice communication systems (now part of Kasten Chase Applied Research). Senior Vice President in charge of research and development for wireless products. Founding director of Call-Net.

Thomas E. Weigman: Lehigh University civil engineer and MBA graduate from University of Pennsylvania. Extensive marketing and sales experience with several companies. Joined Sprint Communications Company in 1991 in long distance marketing. President of consumer services group at Sprint Corp.

Lauren F. Wright: Harvard Business School MBA. Held management positions in corporate finance and treasury, investor relations, and materials and service management with Sprint Communications Company. Currently Vice President and General Manager of Sprint Corp.'s long distance international operations.

Historical operating performance *($ millions)*



($ millions)

	1992	1993	1994	1995	1996
Revenue	82.8	133.9	176.3	457.5	712.6
Gross Profit	31.2	45.1	51.2	155.5	267.9
EBITDA	8.4	8.8	(31.1)	(15.7)	43.1
Net Income (Loss)	1.7	(3.1)	(55.5)	(64.7)	(7.1)
Capital Assets	24.3	44.5	85.3	132.0	169.7

Revenue/ Capital Assets	3.4	3.0	2.1	3.5	4.2
Gross Margin (% of revenue)	37.7%	33.7%	29.0%	34.0%	37.6%
Operating Costs (% of revenue)	27.5%	27.1%	46.7%	37.4%	31.5%
Billed Minutes (in millions)	240	430	720	1,650	2,811

Call-Net's strategy is to capitalize on opportunities in telecommunications arising from regulatory and technological changes.

As barriers to long distance competition were removed over the past five years, we offered new services to business and residential customers across Canada. Today, our wholly-owned subsidiary, Sprint Canada Inc., is the number one long distance alternative to the former monopoly telephone companies.

We also have 19 percent ownership of Microcell Telecommunications Inc., a company we founded in 1992. Microcell is one of two new companies licensed to build national digital wireless telecommunications networks to provide personal communications service, or PCS.

In 1996, we made initial investments in the development of local, mobile wireless and on-line services for potential introduction to customers over the next two years. However, our operating revenues to date are derived solely from long distance services.

THE CANADIAN TELECOMMUNICATIONS MARKETPLACE

Historically, nine provincial and regional monopolists have controlled Canada's telecommunications, with cellular telephony under a duopoly.

Long distance competition began when Call-Net offered enhanced services resale in 1987. The CRTC approved simple resale in 1990 and facilities-based competition in 1992. Full long distance competition commenced in July 1994 when equal access to the public telephone system was implemented.

While competition created an initial influx of new entrants, industry consolidation followed between 1993 and 1995. Only four major alternative long distance companies have survived to compete nationally against an alliance of the telephone companies. The Stentor alliance still dominates the long distance sector with a greater than 70 percent market share. Sprint Canada leads the alternative suppliers with a nine percent share.

Unlike the situation in the United States, where the regional local telephone companies are entering the long distance sector, no major new competitors are expected in the Canadian long distance market. However, despite a 30 to 40 percent drop in rates since mid-1994, the market is expected to grow by six to seven percent a year and should total almost $11 billion in annual revenues by 2000.

The next area of greatest opportunity for competitive entry is expected to be local services. The CRTC is expected to set the terms and conditions of entry in 1997 and the current monopolists are likely to face competition from the alternative long distance companies, the cable companies, and the new wireless services such as PCS and LMCS (local multipoint communications service). Canadian businesses and consumers are expected to increase spend-

ing on local services by eight percent annually to $10 billion by 2000.

The duopoly mobile wireless sector is opening to further competition with two PCS companies currently establishing national service. The mobile wireless services market is expected to expand by 19 percent annually and should generate nearly $6 billion in revenues by 2000, offering opportunities for the bundling of paging and mobile telephony services with long distance and local telephone service.

A fast growing sector is on-line and Internet services with annual growth rates expected to exceed 40 percent over the next few years. Revenues are projected to reach $2 billion annually by 2000. The sector is currently crowded with service providers and substantial consolidation is expected. Integrated carriers and multi-service telecom suppliers are likely to emerge as the leaders.

The expansion of telecommunications competition into more sectors will create several growth opportunities for a well-positioned, low-cost company like Call-Net.

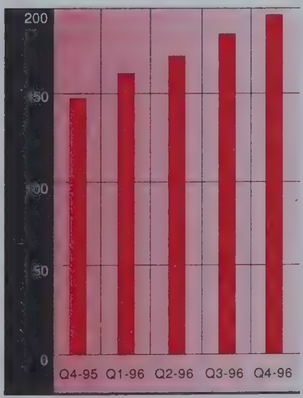
FINANCIAL RESULTS

Strong revenue gains in 1996 far outpaced higher carrier charges and operating expenses as we leveraged the assets put in place in late 1994 and 1995. With EBITDA rising in each quarter throughout 1996, a modest net income was achieved in the third and fourth quarters.

REVENUE AND TRAFFIC VOLUME

Revenue totalled $712.6 million in 1996, a 56 percent increase over the $457.5 million reported in 1995.

Revenue *($ millions)*



During the past five years, our revenue has multiplied nearly nine-fold in response to regulatory changes that encouraged long distance competition. The volume of voice and data traffic carried on our national service has escalated, reaching 2.8 billion billed minutes in 1996 – a 70 percent increase from 1995 and a 12-fold increase in five years. The faster growth in billed minutes compared with revenue reflects the effect of competition on prices as well as changes in our traffic mix. In 1995, residential traffic rose rapidly. In 1996, residential and business traffic grew quarter over quarter at comparable rates, along with revenue derived from business data services.

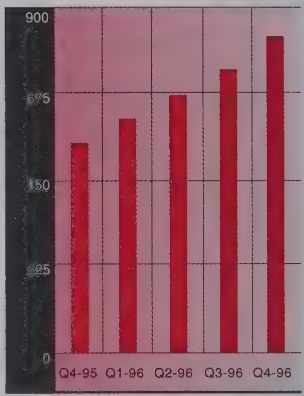
In contrast to the 1993 to 1995 period, when we completed five acquisitions, revenue growth in 1996 was internally generated. No acquisitions were made in 1996; rather, we expanded residential and business customer revenues through focused sales and marketing programs. In particular, we gained recognition from major telecom users impressed by the reliability and global reach of our voice, data and network management services.

In the last two months of 1996, we earned revenue for the first time from Saskatchewan when it was finally opened to competition. We now provide service in all 10 provinces.

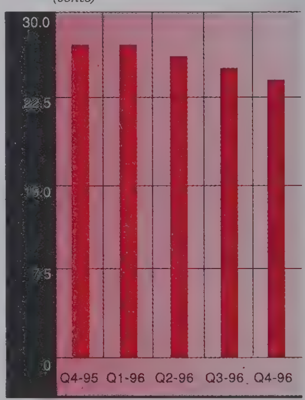
On a quarterly basis, revenue increased in every period during 1996 with the fourth quarter revenue 33 percent higher than the corresponding period in 1995.

Revenue per minute averaged 25.4 cents for the year, compared with 27.7 cents in 1995. The eight percent decline reflected a variety of factors, including changes in product and traffic mix as well as price reductions for some services.

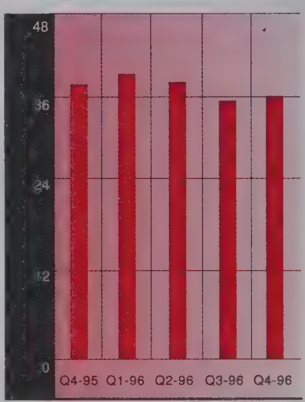
Billed minutes *(millions)*



Revenue per billed minute *(cents)*



Gross margin *(% of revenue)*



CARRIER CHARGES AND GROSS MARGIN

While revenue grew by 56 percent, carrier charges rose by only 47 percent to $444.7 million, producing a gross profit of $267.9 million, a 72 percent improvement over 1995. As a percentage of revenue, gross margin improved to 38 percent from 34 percent a year earlier. Four factors contributed to the improvement.

First, base contribution rates payable to the Stentor companies to subsidize local telephone rates declined by 25 percent. This followed a 20 percent decline in 1995. The 1996 reduction was offset somewhat by a mid-year regulatory change in the method of assessing contribution. Effective June 1, 1996, contribution charges for trunk side access are based on minutes of traffic rather than each circuit used to access the public telephone system. This change increased carrier charges in the third and fourth quarters and reduced our gross margins compared with the first two quarters of 1996. To mitigate these increases, we re-optimized our network in the second half of 1996 to take advantage of other forms of interconnection, including line side access.

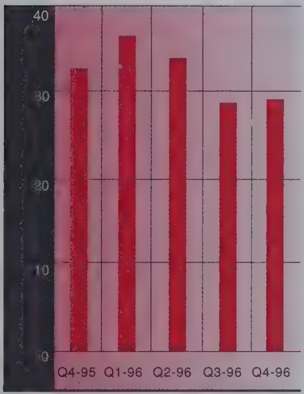
For 1997, base contribution rates charged to the Company will again be reduced at the beginning of the year. The subsidies required to support local services continue to decline due to local rate increases and increased telco operating efficiency. However, the resulting decline in costs will be partially offset in mid-year 1997 by the application of a per minute contribution levy for line side access to the public telephone system. We expect to re-optimize our network once again to limit this mid-year increase.

Second, we enjoyed savings in private line leasing costs through further deployment of our own fibre routes. The construction of circuits in certain high-traffic corridors was completed in 1995 and augmented during 1996 by both fibre swaps and new construction in other areas.

Third, toll costs were lower on a per minute basis, reflecting a more competitive environment for terminating calls off our network.

Fourth, better utilization of the leased elements of our telecommunications network underpinned year over year gross margin improvements.

Operating costs *(% of revenue)*



OPERATING COSTS

Operating costs rose by 31 percent in 1996 to total $224.8 million. This increase lagged far behind the 56 percent expansion in revenue and the 72 percent improvement in gross margin. Operating costs averaged 32 percent of revenue, compared with 37 percent in 1995.

In 1994, the Company made the deliberate decision to invest in growing our revenue base by entering new geographic markets and penetrating a broader range of user segments, particularly the residential segment. The Company does not generally capitalize sales and marketing costs. Most costs incurred in the general course of business, except fixed asset acquisitions, are expensed, consistent with the goal of building shareholder value through conservative management of the balance sheet.

Our expansion strategy resulted in operating costs peaking at 64 percent of revenue in the fourth quarter of 1994 and declining persistently since. They rose slightly to 36 percent of revenue in the first quarter of 1996 compared with the closing quarter of 1995 before declining to the 28 to 29 percent level in the latter part of the year.

The efficiency trend during 1996 is accentuated by the cost of operations per billed minute, which fell from 9.8 cents in the first quarter to 6.9 cents by the fourth quarter.

Another important measure of efficiency is revenue per employee. At the 1996 year end, annualized revenue per employee was approximately $550,000, compared with $500,000 a year earlier. Our staff has expanded rapidly in recent years in response to customer demands and we concluded 1996 with over 1,400 employees.

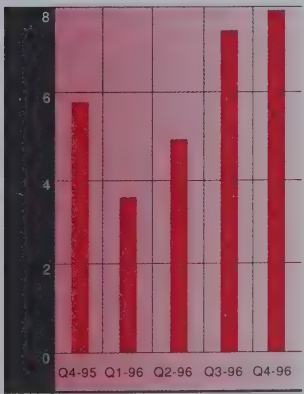
PROFITABILITY

The strategic decision to invest heavily during the second half of 1994 and throughout 1995 in building our long distance business resulted in achieving net income profitability sooner than anticipated.

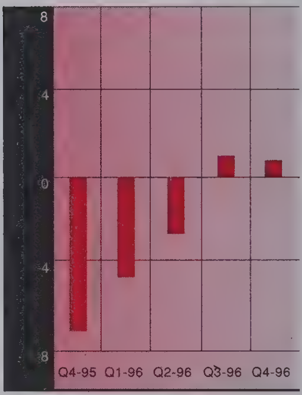
Early in 1996, we did not anticipate achieving a profitable quarter until 1997. However, two quarters of modest net income were reported in the latter half of 1996. Underpinning this profitability are strong revenue growth, investments in network assets to reduce carrier costs, and tight control of selling, general and administrative expense in relation to revenue.

EBITDA (earnings before interest, taxes, depreciation and amortization) showed a $58.8 million year-on-year improvement from a $15.7 million deficiency in 1995 to a positive $43.1 million in 1996. The improvement mounted quarter by quarter and is evident in the upward trend for EBITDA as a percentage of revenue (from six percent in the fourth quarter of 1995 to eight percent in the fourth quarter of 1996).

EBITDA *(% of revenue)*



Net income (loss) *($ millions)*



Call-Net reported a net loss of $7.1 million, or 14 cents per share, in 1996, compared with a loss of $64.7 million, or $1.58 per share, in 1995. The loss diminished during the first half of 1996 to produce modest net income in each of the final two quarters.

DEPRECIATION AND AMORTIZATION

Depreciation and amortization increased by 16 percent, or $4.5 million to $33.2 million, reflecting a $59.7 million increase in capital assets during the year. There was no increase in intangible assets.

INTEREST EXPENSE

Interest expense of $26.1 million in 1996 mostly consisted of accrued interest on U.S. denominated Senior Discount Notes issued in November 1994. Annual interest expense in 1995 was $27.4 million.

The Company maintains a policy of investing surplus cash in highly liquid, secure money market instruments. At December 31, 1996, the investment portfolio exceeded $170 million. Interest income for the year was $9.1 million, compared with $7.1 million in 1995.

LIQUIDITY AND CAPITAL RESOURCES

Call-Net is well capitalized, with more than $170 million of cash on hand, supported by unused credit facilities. This, along with positive cash flow from its long distance operations, will allow the Company to fund its future growth.

CAPITALIZATION

No changes occurred in the capital structure in 1996, except for the issuance of shares as a result of stock option exercises.

Call-Net has visited capital markets five times over the past five years. We completed our $30.4 million initial public share offering in December 1992, followed by two equity offerings in 1993 that netted $120.3 million. These funds were primarily used to finance operations and acquisitions.

In 1994, we raised U.S.$190.1 million from Senior Discount Notes for net proceeds of C$132.9 million. The notes mature in December 2004 and no cash interest is payable prior to December 1999. The Company has hedged a significant portion of its foreign currency exposure through cross-currency swaps.

In 1995, we raised a further $107.9 million in equity capital.

Cash flow from operations
($ millions)

CASH FLOW

Cash flow from operations before working capital changes totaled $51.6 million, compared with a deficiency of $13.4 million in 1995. Following the heavy investment in 1994 and 1995, we have registered five consecutive quarters of rising cash flow, beginning in the fourth quarter of 1995. We expect our long distance business to start generating free cash flow during 1997.

Cash flow from operations after working capital changes was $51.5 million, compared with a $6.3 million shortfall in 1995.

CAPITAL EXPENDITURES

Capital expenditures totaled $59.7 million in 1996, compared with $60.7 million in 1995. In 1996, we expanded the Company-owned fibre network and further upgraded internal infrastructure, including core information management systems to handle the invoicing and reporting requirements of a much expanded customer base. Additional commitments for office space and leasehold improvements were assumed at a new head office in Toronto to accommodate staff and facilities expansion.

Net capital assets grew by $37.7 million to total $169.7 million at year end. Assets include major switching equipment in Vancouver, Calgary, Montreal and Toronto, Company-owned fibre optic circuits, a national data network management centre in Vancouver, a national voice network management centre in Toronto, two customer service centres, information management systems, and 17 offices across Canada.

Although revenue expanded by 56 percent in 1996, net capital assets rose by only 29 percent, leading to improved capital efficiency. Every $100 of net capital assets supported revenue of $420 in 1996, compared with $347 in 1995 and $207 in 1994.

Annualized revenue/ Capital assets

YEAR-END POSITION

Call-Net concluded 1996 with $170.1 million of cash and short-term investments. These funds, combined with the limited cash requirements for our long distance business, will help to finance our entry into local, mobile wireless and on-line services.

Long-term debt of $188.3 million and shareholders' equity of $253.0 million resulted in a debt-to-equity ratio of 0.74:1, compared with 0.67:1 at the end of 1995.

Call-Net's credit facility with its principal bank was unused as at December 31, 1996. The $50.0 million facility was increased to $75.0 million early in 1997.

INVESTMENTS

We own 19 percent of Microcell Telecommunications Inc., a Montreal-based company that was awarded a federal licence in December 1995 to develop a digital wireless PCS telephone service across Canada. Microcell has raised more than $800 million to finance the build out of its national service over three years.

In 1996, we invested $7.8 million in Microcell, bringing our total investment to $18.1 million. We may be required to invest a further $18.6 million (our 19 percent pro rata share of a $100 million commitment by all Microcell shareholders) before the end of 1998. This commitment will be reduced by any external equity raised by Microcell in the meantime.

RISKS AND RISK MANAGEMENT

Call-Net faces several competitive, regulatory and financial uncertainties. Operating and financial strategies, and the deployment of resources, are designed to reduce these potential risks.

COMPETITIVE RISKS

There are currently five major long distance competitors (the four alternative suppliers and the telephone companies) in each regional or provincial market. Our largest competitors are the vertically-integrated telephone companies that form the Stentor group. These companies continue to dominate long distance and monopolize local services. No major new competitors are expected to enter the long distance sector, although the telephone companies will face new competition in the local market.

We manage competitive risks in long distance – and will do so in local and other areas – by being well funded with a conservative balance sheet; by maintaining our operating and capital costs well below major competitors; by leveraging our relationship with Sprint U.S. to access forward thinking know-how; and by offering products and services with a strong value proposition for customers.

Our entry into the local market is an opportunity without current risk exposure. We will decide what risks to accept once we have assessed the CRTC decision on the terms and conditions of competition.

There is some risk attached to Call-Net's investment in Microcell, which faces competition from two national cellular services and another PCS service. Our risk is limited to the $18.1 million already invested and the $18.6 million committed for 1997 and 1998. We manage this risk exposure by having two Call-Net executives on the Microcell board of directors to provide

strategic oversight, by discouraging undue technological risk, and by encouraging Microcell to be first in the market. The company is about a year ahead of its competitor and should be able to establish a commanding market share position.

LEGAL AND REGULATORY RISKS

The ownership and management of Call-Net and Sprint Canada are subject to the provisions of the Telecommunications Act (Canada). The act restricts foreign ownership of a telecommunications carrier to 20 percent, and indirect ownership through a holding company to 33.3 percent. A carrier cannot be otherwise controlled by a foreign entity. Call-Net and Sprint Canada are in compliance with these ownership and control requirements.

The CRTC regulates the long distance and local rates of the Stentor companies, which directly and indirectly affects the rates of Call-Net's existing and proposed operations. Among outstanding regulatory issues are rate rebalancing to eliminate the subsidization of local rates by long distance rates, price cap regulation of Stentor's local services and forbearance of regulation of Stentor's toll services. The CRTC also regulates the contribution charges that Sprint Canada must pay so that it can compete in the long distance market. Contribution payments to Stentor subsidize local service rates. Since 1996, the charge is levied on each minute of traffic for certain types of interconnectivity.

The CRTC is supportive of long distance competition and, as noted, is currently holding a proceeding with a view to opening local telephone service to competition. Call-Net proposes to enter local service, which will be subject to federal regulation.

FINANCIAL RISKS

Call-Net's cash flow from operations has been insufficient to fund all of Sprint Canada's operating and capital expenditures. In 1997, our long distance business should start to generate free cash flow, moving toward a self-funding status. Call-Net has successfully visited capital markets five times since 1992 and expects to raise further capital in 1997 or 1998 to fund its entry into new services. The Senior Discount Notes place limits on the amount of additional debt Call-Net may assume.

The balance sheet continues to be managed conservatively, with a debt to equity ratio of 0.74:1 and cash of $170.1 million at the end of 1996. Some risk is attached to our Senior Discount Notes, although the majority of the foreign currency exposure is hedged. Our bank credit line was increased by 50 percent in early 1997 to $75.0 million.

FUTURE EXPECTATIONS

The management of Call-Net remains focused on achieving superior long-term shareholder returns through the growth of its long distance services and by providing other telecommunications services to our expanding customer base.

At the 1996 year end, our annualized revenue from long distance services approached $800 million. We anticipate continued strong growth in the consumer and business sectors. In February 1997, Sprint Canada introduced Canada's first flat pricing rate plan for consumers and small businesses. This initiative is expected to spur domestic revenues.

In 1997 and 1998, we expect to expand our telecommunications products to include local, mobile wireless and on-line services. This expansion will be supported by many existing advantages:

- a national presence in all market segments;
- a loyal customer base of 820,000 households and more than 60,000 business accounts;
- a low-cost service structure and a low level of embedded capital;
- a strong balance sheet;
- the ability to leverage existing investments in network and network management, customer lists, billing systems, sales distribution channels, customer service call centres and other assets; and
- a market-driven, customer focused work force.

Looking forward, we expect continued strong growth in revenue and EBITDA from long distance services as we strive to meet our goal of 15 percent market share by the year 2000. Consolidated EBITDA growth will be tempered over the next three to four years, as we enter a period of operating and capital investment to gain revenues and build market share by offering new telecommunications services. These expenditures, however, will be made in the usual cautious fashion, taking only a prudent amount of risk, leading to longer term returns and profitability.

MANAGEMENT'S REPORT

Management is responsible for the preparation and presentation of the consolidated financial statements and all other information in the annual report. This responsibility includes the selection of appropriate accounting methods, in addition to making the judgements and estimates necessary to prepare financial statements in accordance with generally accepted accounting principles. It also includes ensuring that the other financial information presented elsewhere in the annual report is consistent with the financial statements.

To safeguard assets and to provide reasonable assurance that relevant and reliable financial information is being produced, management maintains a system of internal controls. The financial statements have been audited by the independent shareholders' auditors, Ernst & Young, whose report follows.

The Board of Directors, acting through an Audit Committee, is responsible for determining that management fulfills its responsibilities in the preparation of financial statements and the financial control of operations. The Board of Directors recommends the independent auditors for appointment by the shareholders. The Audit Committee meets regularly with financial management and the independent auditors to discuss internal controls, auditing matters and financial reporting issues. The independent auditors have unrestricted access to the Audit Committee. The Committee reviewed the consolidated financial statements and management's discussion and analysis prior to the Board approving them for inclusion in the annual report.

Juri Koor

Juri Koor *President and Chief Executive Officer*

Jim Hardy *Vice President and Chief Financial Officer*

AUDITORS' REPORT

To the Shareholders of

Call-Net Enterprises Inc.

We have audited the consolidated balance sheets of **Call-Net Enterprises Inc.** as at December 31, 1996 and 1995 and the consolidated statements of operations and deficit and cash flows for each of the years in the three-year period ended December 31, 1996. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1996 and 1995 and the results of its operations and the changes in its financial position for each of the years in the three-year period ended December 31, 1996 in accordance with accounting principles generally accepted in Canada.

Ernst + Young

Ernst & Young *Chartered Accountants*

Toronto, Canada,
February 13, 1997

CONSOLIDATED BALANCE SHEETS

As at December 31 (millions of Canadian dollars)	**1996**	1995
ASSETS		
Cash and short-term investments	**170.1**	179.6
Accounts receivable	**117.8**	90.9
Prepaid expenses and deposits	**1.9**	1.8
Total current assets	**289.8**	272.3
Capital assets [note 3]	**169.7**	132.0
Investment [note 4]	**18.1**	10.3
Other assets [note 5]	**97.9**	110.2
Total assets	**575.5**	524.8
LIABILITIES AND SHAREHOLDERS' EQUITY		
Accounts payable and accrued liabilities	**131.3**	104.4
Current portion of long-term debt [note 7]	**—**	0.2
Current portion of capital lease obligations [note 8]	**2.9**	2.6
Total current liabilities	**134.2**	107.2
Long-term debt		
Long-term debt [note 7]	**186.0**	164.6
Capital lease obligations [note 8]	**2.3**	3.5
Total long-term debt	**188.3**	168.1
Contingencies [note 13]		
Shareholders' equity		
Capital stock [note 9]		
Common Shares, unlimited authorized	**122.8**	119.9
Class B Non-Voting Shares, unlimited authorized	**142.9**	135.2
Class C Non-Voting Shares, unlimited authorized	**117.5**	117.5
Deficit	**(130.2)**	(123.1)
Total shareholders' equity	**253.0**	249.5
Total liabilities and shareholders' equity	**575.5**	524.8

See accompanying notes

On behalf of the Board:

Director

Director

CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT

Years ended December 31 (millions of Canadian dollars, except per share amounts)	**1996**	1995	1994
Revenues	**712.6**	457.5	176.3
Carrier charges	**444.7**	302.0	125.1
Gross profit	**267.9**	155.5	51.2
Operating costs	**224.8**	171.2	82.3
Earnings (loss) before interest, taxes, depreciation and amortization	**43.1**	(15.7)	(31.1)
Depreciation and amortization	**(33.2)**	(28.7)	(24.4)
Operating income (loss)	**9.9**	(44.4)	(55.5)
Interest on long-term debt and capital leases	**(26.1)**	(27.4)	(3.8)
Interest and investment income	**9.1**	7.1	3.9
Net income (loss) for the year	**(7.1)**	(64.7)	(55.4)
Deficit, beginning of year	**(123.1)**	(58.4)	(3.0)
Deficit, end of year	**(130.2)**	(123.1)	(58.4)
Earnings (loss) per share [note 15]	**(0.14)**	(1.58)	(1.62)

See accompanying notes

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31 (millions of Canadian dollars)	**1996**	1995	1994
OPERATING ACTIVITIES			
Net income (loss) for the year	**(7.1)**	(64.7)	(55.4)
Add operating items not requiring cash			
Depreciation and amortization	**33.2**	28.7	24.4
Interest on long-term debt	**25.5**	21.8	2.0
Loss on write-down of investment	**—**	0.8	—
Cash flow from operations before changes in non-cash working capital	**51.6**	(13.4)	(29.0)
Changes in non-cash working capital balances related to operations [note 11]	**(0.1)**	7.1	15.5
Cash provided by (used in) operating activities	**51.5**	(6.3)	(13.5)
INVESTING ACTIVITIES			
Acquisition of capital assets	**(59.7)**	(60.7)	(52.0)
Investment in Microcell Telecommunications Inc. [note 4]	**(7.8)**	(6.7)	(3.0)
Investment in In-Flight Phone Canada Inc.	**—**	(0.2)	(0.6)
Purchase of STN assets [note 2]	**—**	(19.0)	—
Purchase of Airway Broadcasting assets [note 2]	**—**	(0.9)	(0.9)
Purchase of Insinc [note 2]	**—**	—	(26.8)
Other assets	**0.3**	(1.2)	(0.4)
Cash used in investing activities	**(67.2)**	(88.7)	(83.7)
FINANCING ACTIVITIES			
Issue of capital stock	**10.6**	109.9	36.7
Obligations under capital leases	**1.9**	5.3	—
Repayment of capital leases	**(2.8)**	(1.7)	(1.6)
Issuance of long-term debt	**—**	3.5	137.7
Repayment of long-term debt	**(3.5)**	(0.1)	(10.0)
Debt issue costs	**—**	—	(5.8)
Cash provided by financing activities	**6.2**	116.9	157.0
Net increase (decrease) in cash during the year	**(9.5)**	21.9	59.8
Cash acquired on the purchase of Insinc [note 2]	**—**	—	7.5
Cash and short-term investments, beginning of year	**179.6**	157.7	90.4
Cash and short-term investments, end of year	**170.1**	179.6	157.7

See accompanying notes

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada. These principles are also in conformity in all material respects with accounting principles generally accepted in the United States except as described in note 17 to the consolidated financial statements.

Principles of Consolidation

The consolidated financial statements include the accounts of Call-Net Enterprises Inc. and its principal operating subsidiaries Sprint Canada Inc. and Call-Net Communications Inc., hereafter referred to as the "Company".

The Company owns approximately 19% of the shares of Microcell Telecommunications Inc. ("Microcell"). This investment is accounted for using the cost basis as the Company believes it does not exert significant influence over the affairs of Microcell.

Cash and Short-Term Investments

Short-term investments are recorded at cost, which approximates market value.

Capital Assets

Capital assets are recorded at cost. Depreciation on all assets commences when the assets are put into service. Depreciation and amortization are being provided based on the estimated useful lives of the assets on a straight-line basis as follows:

Buildings	40 years
Fibre optic cable and equipment	20 years
Multiplex and telephone switch equipment	10 years
Computer equipment and software	3 to 5 years
Furniture and fixtures	5 years
Leasehold improvements	term of the lease
Equipment under capital lease	term of the lease, not exceeding estimated useful life

Investments

Investments are recorded at cost.

Investments are valued on a quarterly basis by estimating future net undiscounted cash flows and residual values or by reviewing the business and operating plans of investee companies. Any decline in the value of an investment that is other than a temporary decline results in the investment being written down with a charge against income.

Other Assets

Goodwill Goodwill, which represents the excess of the purchase price of the Company's interest in subsidiary companies over the fair value of the underlying net identifiable assets of the business acquired, is being amortized on a straight-line basis over 20 years.

Goodwill is assessed for future recoverability or impairment on an annual basis by estimating future net undiscounted cash flows and residual values. Any permanent impairment of the value of the unamortized portion of goodwill is written down with a charge against income.

Intangible Assets Technology and product rights, customer lists, trademarks and other intangible assets are recorded at cost.

Intangible assets are assessed for future recoverability or impairment on an annual basis by estimating future net undiscounted cash flows and residual values or by estimating replacement or appraised values. When the net carrying amount of an intangible asset exceeds the estimated net recoverable amount, the asset is written down with a charge against income.

Amortization of intangible assets is being recorded on a straight-line basis as follows:

Technology and product rights	10 years
Customer lists	10 years
Trademarks	10 years
Financing costs	term of the financing

Capital Leases

Leases which transfer substantially all the benefits and risks of ownership of the leased asset to the Company are capitalized by recording the present value of future payments under the lease as an asset and a liability on the balance sheet. Capitalized leased assets are amortized over their estimated useful lives on a basis consistent with owned assets and lease payments are applied to a reduction in the amount of the obligation and to interest expense over the term of the lease.

Foreign Currency

Monetary assets and liabilities in U.S. dollars are translated into Canadian dollars at the year-end rate of exchange and any gains or losses are reflected in income. Revenues and expenses are translated into Canadian dollars at the rate of exchange prevailing at the time of the transaction.

Derivative Financial Instruments

The Company purchases services from U.S. based telephone carriers to terminate southbound traffic in the normal course of business. The peak liability during the year was approximately $33.8. The Company has a foreign exchange hedge program including use of forward exchange contracts to manage the risk of this foreign currency denominated liability. Exchange gains or losses associated with this program are included in income as incurred.

The Company is party to long-term cross-currency interest rate swap agreements to manage risks associated with the Senior Discount Notes. Any net cost or benefit associated with such agreements is recorded on an accrual basis as an adjustment to interest expense. The costs associated with entering into the cross-currency interest rate swaps are being amortized over the term of the loan on a straight-line basis.

The principal amount of the related Senior Discount Notes has been translated into Canadian dollars at the year-end rate of exchange. The effect of the cross-currency interest rate swap agreements entered to hedge this liability is included in assets in the case of favourable contracts and liabilities in case of unfavourable contracts.

The unhedged accrued interest on the Senior Discount Notes has been translated during the year at month-end exchange rates. At the end of the year, the total accrued interest has been adjusted to reflect the year-end exchange rate. The resulting foreign exchange gain or loss has been deferred and is being amortized over the remaining period to maturity.

2. ACQUISITIONS

1995 Transactions:

Smart Talk Network Inc. ["STN"] Effective August 4, 1995, the Company acquired certain assets of STN, a competitor that was in bankruptcy proceedings. The purchase price of $19.0 was paid in cash and has been allocated to the assets acquired based on their estimated fair market values as follows: working capital $9.0, customer lists and product rights $9.0, and capital assets $1.0. The acquisition has been accounted for using the purchase method, with the results of operations being included in these consolidated financial statements from the date of acquisition.

1994 Transactions:

Integrated Network Services Inc. ["Insinc"] On December 5, 1994, the Company acquired all the outstanding shares of Insinc. Consideration given for the purchase consisted of 4,245,597 Class B Non-Voting Shares having a fair market value of $26.8. The purchase price has been allocated to the net assets acquired based on estimated fair market values as follows: cash $7.5, working capital deficiency $2.7, capital assets $3.6, goodwill $19.1, and capital lease obligations $0.7. The acquisition has been accounted for using the purchase method, with the results of operations being included in these consolidated financial statements from the date of acquisition.

Airway Broadcasting Company Limited ["Airway Broadcasting"] On July 27, 1994, the Company acquired the long-distance business of Airway Broadcasting for cash of $0.9. During 1995, additional consideration based on performance of $0.9 was paid in cash. The purchase price has been allocated to customer lists and product rights based on fair market values.

3. CAPITAL ASSETS

	1996			1995		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Multiplex & telephone switch equipment	**98.0**	**20.6**	**77.4**	63.4	13.3	50.1
Fibre optic cable & equipment	**50.0**	**3.8**	**46.2**	44.6	1.5	43.1
Computer equipment & software	**40.2**	**17.5**	**22.7**	27.5	9.2	18.3
Leasehold improvements	**12.4**	**4.0**	**8.4**	8.9	2.5	6.4
Furniture and fixtures	**15.4**	**6.1**	**9.3**	12.8	3.7	9.1
Buildings	**5.4**	**0.2**	**5.2**	4.5	—	4.5
Land	**0.5**	**—**	**0.5**	0.5	—	0.5
	221.9	**52.2**	**169.7**	162.2	30.2	132.0

Included in the above is equipment under capital leases for computer equipment with a cost at December 31, 1996 of $8.6 [1995 – $6.7] and accumulated amortization of $1.8 [1995 – $0.4].

4. INVESTMENT

	1996	1995
Investment in Microcell	**18.1**	10.3

During 1996, the Company acquired 1,505,133 shares of Microcell for cash consideration of $7.8 and a commitment collateralized by the 1,505,133 shares issued to invest up to an additional $18.6 in Microcell upon request at any time until December 31, 1998. As a result of this transaction, the Company maintained its 19% interest in Microcell. During 1995, an additional cash investment of $6.7 was made in Microcell.

5. OTHER ASSETS

	1996			1995		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Technology and product rights	**50.8**	**15.8**	**35.0**	50.8	10.8	40.0
Customer lists	**28.5**	**8.1**	**20.4**	28.5	5.3	23.2
Trademarks	**14.9**	**4.5**	**10.4**	14.9	3.0	11.9
Goodwill	**29.7**	**4.2**	**25.5**	29.7	2.7	27.0
Financing costs	**7.0**	**2.3**	**4.7**	6.8	1.4	5.4
Other deferred costs	**3.1**	**1.2**	**1.9**	3.6	0.9	2.7
	134.0	**36.1**	**97.9**	134.3	24.1	110.2

6. OPERATING LINE OF CREDIT

Subsequent to year end, the Company entered into an amended loan agreement with a syndicate of banks increasing its credit facility to $75 and replacing a previous loan agreement with its bank whereby it was provided with a credit facility of $50 under which no amount had been drawn at December 31, 1996 [1995 – nil].

Amounts advanced under either credit facility bear interest at rates varying from the bank prime rate plus 0.5% per annum and the Bankers' Acceptance rate plus 1.5% per annum. Access to the credit facility is subject only to advances not exceeding 70% of accounts receivable under 90 days old. Borrowings under either facility are collateralized by charges over accounts receivable.

7. LONG-TERM DEBT

	1996	1995
Loans payable	**—**	3.5
Senior Discount Notes	**186.0**	161.3
	186.0	164.8
Less current portion	**—**	0.2
	186.0	164.6

Loans Payable

During 1995, the Company obtained term loan financing totalling $3.5 in connection with the purchase of two properties. The loan was repaid in August 1996 without penalty.

Senior Discount Notes

In November 1994, the Company completed an offering of U.S. $190.1 Senior Discount Notes [the "Notes"] for cash proceeds of $137.7 [U.S. $100.0] which after underwriting and issue costs resulted in net proceeds of approximately $132.9 [U.S. $96.5]. The Notes mature in December 2004.

The Notes are senior unsecured obligations of the Company, ranking equally with other unsecured and unsubordinated indebtedness. The Notes have a 13.25% yield to maturity calculated on a semi-annual bond equivalent basis. The Notes were issued at a 52.595% discount from their principal amount, reflecting that no cash interest will be payable prior to December 1, 1999. Thereafter, cash interest will accrue at a rate of 13.25% per annum and will be payable on each of June 1 and December 1, commencing June 1, 2000. The Notes are redeemable at the option of the Company, in whole or in part, at any time on or after December 1, 1999 at 106.625% of the principal amount, declining ratably to 100% of the principal amount on or after December 1, 2002, plus, in each case, interest accrued to the date of redemption. The Notes are governed by a trust indenture which contains certain covenants, which, among other things, will restrict the ability of the Company to incur additional indebtedness, pay dividends, or repurchase the Company's capital stock.

To hedge this obligation, the Company entered into long-term cross-currency interest rate swap

agreements to reduce the Company's exposure to additional changes in the exchange rate of the U.S. dollar as compared to the Canadian dollar. The effect of these agreements is to convert the Notes from a U.S. dollar obligation yielding 13.25% into a 14.13% Canadian dollar obligation, calculated on a yield equivalent basis.

The Company's obligations under the cross-currency interest rate swap agreements are collateralized by charges over accounts receivable.

8. CAPITAL LEASE OBLIGATIONS

The Company has entered into various capital leases for computer equipment with imputed interest rates that range from 6.4% to 13.2% and expiry dates to December 1999. The following is a schedule of future minimum lease payments under the capital leases together with the balance of the obligation under the capital leases:

	1996	1995
1996	**—**	3.0
1997	**3.2**	2.5
1998	**1.8**	1.3
1999	**0.6**	0.1
	5.6	6.9
Less amount representing interest	**0.4**	0.8
	5.2	6.1
Less current portion	**2.9**	2.6
	2.3	3.5

9. CAPITAL STOCK

Certain restrictions on the payment of dividends exist as a result of the Senior Discount Notes issued in 1994 [note 7].

Common Shares

The Company is authorized to issue an unlimited number of Common Shares. The holders of Common Shares are entitled to one vote for each share held at any meeting of shareholders of the Company. The Common Shares may be subject to constraints on transfer to ensure the Company's compliance with the foreign ownership provisions of the Telecommunications Act [Canada].

Preference Shares

The Company is authorized to issue in series an unlimited number of Preferred Shares of which none were outstanding at December 31, 1996, 1995 and 1994.

Class B Non-Voting Shares

The Class B Non-Voting Shares were created in October 1993 when each Common Share then outstanding was converted into one Common Share and one Class B Non-Voting Share.

The Class B Non-Voting Shares rank *pari passu* with Common Shares and Class C Non-Voting Shares on a per share basis with respect to the payment of dividends and the right to participate in a distribution of assets of the Company on winding up, dissolution or otherwise. The holders of Class B Non-Voting Shares are not entitled to vote at any meeting of shareholders of the Company.

Class C Non-Voting Shares

The Class C Non-Voting Shares may not be held by parties other than Sprint U.S., its affiliates and permitted associates. The Class C Non-Voting Shares rank *pari passu* with Common Shares and Class B Non-Voting Shares on a per share basis with respect to the payment of dividends and the right to participate in a distribution of assets of the Company on winding up, dissolution or otherwise. The holders of Class C Non-Voting Shares are not entitled to vote at any meeting of shareholders of the Company. However, the holders of the Class C Non-Voting Shares are entitled to elect up to three directors of the Company as long as they maintain a significant equity interest in the Company.

Number of Shares	Common	Class B	Class C
Balance, December 31, 1993	9,303,746	15,908,746	8,322,664
Issued pursuant to options	108,900	108,900	—
Issued pursuant to Insinc purchase	—	4,245,597	—
Issued to Sprint U.S.	—	—	1,389,409
Balance, December 31, 1994	9,412,646	20,263,243	9,712,073
Issued pursuant to options	10,700	304,541	—
Issued pursuant to underwriters' agreement	6,875,000	—	—
Issued to Sprint U.S.	605,000	—	2,420,000
Balance, December 31, 1995	16,903,346	20,567,784	12,132,073
Issued pursuant to options	472,800	1,050,691	—
Balance, December 31, 1996	**17,376,146**	**21,618,475**	**12,132,073**

Dollars	Common	Class B	Class C
Balance, December 31, 1993	38.4	105.9	81.6
Issued pursuant to options	0.6	0.6	—
Issued pursuant to Insinc purchase	—	26.8	—
Issued to Sprint U.S.	—	—	8.8
Balance, December 31, 1994	39.0	133.3	90.4
Issued pursuant to options	0.1	1.9	—
Issued pursuant to underwriters' agreement	74.3	—	—
Issued to Sprint U.S.	6.5	—	27.1
Balance, December 31, 1995	119.9	135.2	117.5
Issued pursuant to options	2.9	7.7	—
Balance, December 31, 1996	**122.8**	**142.9**	**117.5**

1995 Transactions

On November 8, 1995, pursuant to an agreement with a group of underwriters, the Company issued 7,480,000 Common Shares and 2,420,000 Class C Shares for aggregate net cash proceeds of $107.9. All of the Class C Shares and 605,000 of the Common Shares were purchased by Sprint U.S. in order to maintain its approximate 25% interest in the Company.

1994 Transactions

On December 5, 1994, pursuant to the acquisition of Insinc, the Company issued 4,245,597 Class B Shares having a fair market value of $26.8.

Also on this date, Sprint U.S. exercised its option to maintain a 25% interest in the Company. Accordingly, 1,389,409 Class C Shares were issued for cash proceeds of $8.8.

Stock Options

The outstanding stock options have expiry dates ranging from 1997 to 2004. The following is a continuity of stock options outstanding:

	1996		1995	
	Common	**Class B**	Common	Class B
Balance, beginning of year	**938,818**	**3,435,701**	607,481	2,858,669
Granted during the year	**423,641**	**767,541**	342,037	1,301,321
Cancelled during the year	**—**	**(462,654)**	—	(419,748)
Exercised during the year	**(472,800)**	**(1,050,691)**	(10,700)	(304,541)
Balance, end of year	**889,659**	**2,689,897**	938,818	3,435,701
Weighted average exercise price per share on outstanding options at end of year	**$11.83**	**$10.49**	$7.97	$8.44

All options of the Company are now granted pursuant to a Director and Employee Stock Option Plan from shares reserved for issuance upon the exercise of options granted under such Plan. Both the Plan and the number of shares reserved for issuance under the plan were approved at the Company's Annual General Meeting on June 11, 1996. The Plan reserves 1,890,333 Common Shares and 4,822,189 Class B Non-Voting Shares for issuance upon the exercise of options granted including shares reserved for issuance under options outstanding at the Plan initiation date, December 21, 1995. The number of shares reserved and available for issuance upon the exercise of future options granted is summarized below:

	1996	
	Common	**Class B**
Balance, beginning of year	**951,515**	**1,386,646**
Options granted during the year	**(423,641)**	**(767,541)**
Options cancelled during the year	**—**	**462,654**
Balance, end of year	**527,874**	**1,081,759**

10. INCOME TAXES

At December 31, 1996, the Company had approximately $129.5 [1995 – $121.5] in non-capital loss carryforwards. These amounts are available to reduce future years' taxable income and will expire as follows:

1997	3.9
1998	7.1
1999	4.3
2000	2.7
2001	41.9
2002	60.2
2003	9.4
Total	129.5

11. CHANGES IN NON-CASH WORKING CAPITAL BALANCES RELATED TO OPERATIONS

	1996	1995	1994
Accounts receivable	**(26.9)**	(43.0)	(14.1)
Prepaid expenses and deposits	**(0.1)**	(0.8)	0.2
Accounts payable and accrued liabilities	**26.9**	50.9	29.4
	(0.1)	7.1	15.5

12. FINANCIAL COMMITMENTS

The Company leases office space under operating leases that expire through 2006. The Company also has agreements with certain telephone companies that guarantee the long-term supply of network facilities at discounts to full rates.

The minimum payments under these agreements in aggregate and for each of the next five years and thereafter are as follows:

	Operating Leases	Long Distance Facilities
1997	5.0	31.6
1998	4.7	23.2
1999	4.2	23.2
2000	4.1	21.7
2001	4.0	1.7
Thereafter	18.9	—
	40.9	101.4

13. CONTINGENCIES

In the ordinary course of business activities, the Company may be contingently liable for litigation and claims with customers and suppliers. Management believes that adequate provisions have been recorded in the accounts where required. Although it is not possible to estimate the potential costs and losses, if any, management believes that the ultimate resolution of such contingencies will not have a material adverse effect on the consolidated financial position of the Company.

14. RELATED PARTY TRANSACTIONS

The Company has engaged in significant sales and purchases of goods and services with related parties for each of the three years ended December 31, 1996 in the normal course of operations under normal trade terms and conditions. At December 31, 1996 the net balance owing to these parties is $33.8 [1995 – $24.6].

15. EARNINGS (LOSS) PER SHARE

Earnings (loss) per share has been calculated on the basis of income (loss) less preference share dividends, divided by the weighted average number of Common Shares, Class B Shares and Class C Shares outstanding during the year [note 9] [1996 – 50,622,652; 1995 – 41,025,289; and 1994 – 34,144,036 after giving retroactive effect to the creation of the Class B Shares during 1993]. The potential exercise of stock options has no current dilutive effect on earnings per share.

16. ADDITIONAL FINANCIAL INFORMATION

Effective January 1, 1996 the Canadian Institute of Chartered Accountants requires that companies disclose in their notes to the financial statements information pertaining to recognized and unrecognized financial instruments to enhance the understanding of the impact financial instruments have on an entity's financial position, performance and cash flows. Following is the information that is required by this new standard that is not provided elsewhere in the financial statements.

Credit Risk

The Company's accounts receivable are not subject to any concentration of credit risk. The portfolio is diversified as to both geographic and industry concentrations.

Cross-currency interest rate swap agreements and foreign currency contracts involve the risk of dealing with counterparties and their ability to meet the terms of the contracts. In the event of non-performance by the counterparties, the Company's accounting loss would be limited to the net amount that it would be entitled to receive under the terms of the applicable cross-currency interest rate swap agreement or foreign currency contract. However, the Company has a policy of only dealing with large, creditworthy financial institutions and, therefore, does not anticipate non-performance by any of the counterparties with which it has such agreements.

Financial Instruments

The carrying amounts and estimated fair values of the Company's financial instruments as of December 31 are as follows:

	1996		1995	
	Carrying Amount	**Estimated Fair Value**	Carrying Amount	Estimated Fair Value
Financial assets				
Cash and short-term investments	**170.1**	**170.1**	179.6	179.6
Accounts receivable	**117.8**	**117.8**	90.9	90.9
Investment in Microcell Telecomunications Inc.	**18.1**	**18.1**	10.3	10.3
Financial liabilities				
Accounts payable and accrued liabilities	**131.3**	**131.3**	104.4	104.4
Long-term debt				
Loans payable	**—**	**—**	3.5	3.5
Senior Discount Notes	**186.0**	**213.7**	161.3	185.4
Capital lease obligations	**5.2**	**5.2**	6.1	6.1
Off-balance sheet instruments				
Cross-currency interest rate swap agreements	**—**	**(26.6)**	—	(5.6)
Foreign currency contracts	**—**	**0.1**	—	—

The fair value of the Company's financial instruments has been determined as follows:

Cash and short-term investments and accounts receivable

The carrying values of the Company's cash and short-term investments and accounts receivable approximate fair value.

Investment in Microcell

The carrying value of the Company's investment in Microcell has been used to approximate fair value since Microcell is a privately owned company for which there is no publicly quoted market price. However, management believes that the fair value of the investment is in excess of carrying value because of the substantial market opportunities available for the PCS technology.

Accounts payable and accrued liabilities

The carrying value of the Company's accounts payable and accrued liabilities approximate fair value.

Long-term debt

The fair value of the Company's long-term debt is estimated based on the quoted market price for the Company's publicly traded Senior Discount Notes. The Company currently has no plan to settle this obligation prior to maturity.

Cross-currency interest rate swap agreements

The notional fair value of cross-currency interest rate swap agreements is estimated as the cost that the Company would pay to terminate the swap agreements at December 31, 1996 and 1995, taking into account the prevailing interest rate and currency environments. However, these agreements are part of a long-term hedging strategy and thus the Company currently has no plans to terminate the agreements prior to their maturity.

Foreign currency contracts

The fair value of foreign currency contracts is estimated as the replacement cost of the contracts at December 31, 1996 and 1995, taking into account the current foreign currency exchange rates.

Cross-currency Interest Rate Swap Agreements

The Company has entered into cross-currency interest rate swap agreements to hedge its exposure to adverse movements in the relationship between the Canadian and U.S. dollars created under the Senior Discount Notes. Of the U.S. $316.0 that will be paid in principal and interest over the 10 year life of this instrument, the Company has hedged approximately 70% of the exposure for the entire term of the notes. The Company feels that this conservative financial policy is necessary to offset the high degree of business risk associated with its primary activities.

Foreign Currency Contracts

The Company purchases over-the-counter forward exchange contracts to hedge the purchase of U.S. dollars needed to settle U.S. dollar denominated trade obligations. The notional amount outstanding on these contracts at December 31, 1996 is U.S. $20.0.

17. RECONCILIATION TO ACCOUNTING PRINCIPLES GENERALLY ACCEPTED IN THE UNITED STATES

These consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada, which differ in certain respects from accounting principles generally accepted in the United States. If United States accounting principles were used, the adjustments described below would be required in the consolidated financial statements.

Balance Sheets – Assets

	1996	1995	1994
Canadian accounting principles			
Cash and short-term investments	**170.1**	179.6	157.7
United States accounting principles			
Cash and cash equivalents	**110.4**	77.3	80.8
Short-term investments available for sale	**59.7**	102.3	76.9

United States accounting principles classify cash and cash equivalents to exclude short-term investments which mature more than three months from the date of their acquisition.

Balance Sheets – Shareholders' Equity

	1996	1995	1994
Capital Stock			
Canadian accounting principles	**383.2**	372.6	262.7
Share purchase incentives	**4.6**	4.6	1.8
Reduction in stated capital	**10.7**	10.7	10.7
United States accounting principles – Capital Stock	**398.5**	387.9	275.2
Deficit			
Canadian accounting principles	**(130.2)**	(123.1)	(58.4)
Share purchase incentives	**(4.6)**	(4.6)	(1.8)
Reduction in stated capital	**(10.7)**	(10.7)	(10.7)
United States accounting principles – Deficit	**(145.5)**	(138.4)	(70.9)

Generally accepted accounting principles in Canada allow for the reduction of the stated capital of outstanding shares with a corresponding offset to deficit. This reclassification which the Company made in 1992 is not permitted by United States accounting principles.

Statements of Operations

	1996	1995	1994
Net income (loss) based on Canadian accounting principles	**(7.1)**	(64.7)	(55.4)
Share purchase incentives	**—**	(2.8)	(0.3)
Net income (loss) based on United States accounting principles	**(7.1)**	(67.5)	(55.7)
Earnings (loss) per share			
Net income (loss) primary	**($0.14)**	($1.61)	($1.59)

Under Canadian accounting principles, stock options are accounted for at the date of exercise when the purchase is recorded as an increase to capital stock. For purposes of reconciliation to United States accounting principles, stock options granted to employees have been accounted for in accordance to APB 25, such that the excess of the market value of the shares over the exercise price is expensed and charged to income with a corresponding increase to capital stock over the vesting period.

Under United States accounting principles, Statement of Financial Accounting Standard No. 109 requires an asset and liability approach to financial accounting for income taxes. A full valuation allowance has been provided for which offsets any deferred tax asset or liability.

Under United States accounting principles, foreign exchange gains or losses from the translation of long-term monetary items are included in income as incurred. Under Canadian accounting principles, foreign exchange gains or losses on the translation of long-term monetary items are deferred and amortized. Any difference resulting from the application of this principle is not significant.

United States accounting principles do not recognize the disclosure of a subtotal of the amount of earnings before interest, taxes and depreciation and amortization in the statements of operations and deficit.

United States accounting principles require the consideration of stock options in the determination of primary earnings per share. The weighted average number of Common, Class B and Class C Shares outstanding for the calculation of primary earnings per share under United States accounting principles are 1996 – 50,623,000 [1995 – 41,941,000 and 1994 – 35,000,000].

Statements of Cash Flows

	1996	1995	1994
Cash provided by (used in) operating activities	**51.5**	(9.1)	(13.8)
Cash used in investing activities	**(24.7)**	(114.1)	(57.9)
Cash provided by financing activities	**6.3**	119.7	130.6
Increase (decrease) in cash	**33.1**	(3.5)	58.9
Cash acquired on the purchase of Insinc	**—**	—	7.5
Cash and cash equivalents, beginning of year	**77.3**	80.8	14.4
Cash and cash equivalents, end of year	**110.4**	77.3	80.8

United States accounting principles do not recognize the disclosure of a subtotal of the amount of funds provided by operations before changes in non-cash working capital items in the statements of cash flows.

United States accounting principles exclude non-cash transactions from the statements of cash flows, including acquisitions for share consideration and the conversion of liabilities to equity.

ADDITIONAL FINANCIAL INFORMATION

Historical Review	1996	1995	1994	1993	1992	1991
Statement of Operations ($MM)						
Revenue	**712.6**	457.5	176.3	133.9	82.8	68.7
Gross Margin	**37.6%**	34.0%	29.0%	33.7%	37.6%	39.5%
EBITDA	**43.1**	(15.7)	(31.1)	8.8	8.4	4.1
Net Income (loss)	**(7.1)**	(64.7)	(55.4)	(3.1)	1.7	(5.0)
Earnings (loss) Per Share	**(0.14)**	(1.58)	(1.62)	(0.16)	0.18	(0.65)
Balance Sheet ($MM)						
Working Capital	**155.6**	165.1	144.4	94.0	27.9	(11.0)
Total Assets	**575.5**	524.8	400.0	254.8	65.6	40.2
Long-term Debt	**188.3**	168.1	140.9	10.8	11.7	11.6
Shareholders' Equity	**253.0**	249.5	204.3	222.9	43.2	5.4

1996 Quarterly Review	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
(Unaudited)	**1996**	1995	**1996**	1995	**1996**	1995	**1996**	1995
Statement of Operations ($MM)								
Revenue	**161.5**	86.0	**171.6**	101.5	**183.9**	123.2	**195.6**	146.8
Gross Margin	**39.7%**	29.1%	**38.6%**	32.9%	**35.9%**	33.3%	**36.6%**	38.2%
EBITDA	**5.6**	(11.7)	**8.3**	(8.3)	**13.7**	(4.2)	**15.5**	8.5
Net Income (loss)	**(5.2)**	(20.9)	**(3.1)**	(18.9)	**0.7**	(17.2)	**0.5**	(7.7)
Earnings (loss) Per Share	**(0.10)**	(0.53)	**(0.06)**	(0.48)	**0.01**	(0.43)	**0.01**	(0.14)
Balance Sheet ($MM)								
Working Capital	**176.8**	115.7	**161.6**	100.9	**158.0**	66.6	**155.6**	165.1
Total Assets	**533.8**	390.5	**554.1**	386.9	**576.8**	398.4	**575.5**	524.8
Long-term Debt	**173.4**	146.2	**178.6**	154.1	**181.0**	163.1	**188.3**	168.1
Shareholders' Equity	**251.8**	183.3	**248.9**	165.9	**249.7**	149.2	**253.0**	249.5

Stock Information	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
	Common	Class B	Common	Class B	Common	Class B	Common	Class B
1996 share price ($) and trading volume								
High	**15.50**	**15.25**	**16.25**	**16.25**	**16.35**	**16.75**	**18.50**	**17.00**
Low	**11.13**	**11.00**	**14.63**	**14.25**	**14.50**	**14.30**	**14.20**	**13.90**
Close	**15.13**	**15.00**	**16.20**	**16.10**	**15.00**	**14.50**	**18.00**	**16.75**
Volume (000s)	**3,616**	**4,478**	**2,655**	**3,028**	**2,094**	**2,392**	**2,520**	**4,605**
1995 share price ($) and trading volume								
High	8.00	8.00	9.60	9.50	12.25	12.63	12.25	12.50
Low	5.88	5.50	7.63	7.38	9.50	9.25	9.25	9.25
Close	7.75	7.50	9.25	9.25	11.88	12.00	11.75	12.50
Volume (000s)	913	1,629	193	1,335	331	3,570	2,756	4,477

CORPORATE DIRECTORY

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Vice President Law

Brock Robertson
Vice President and Treasurer

* Member of Audit Committee
◆ Member of Compensation and Human Resources Committee
▲ Member of Corporate Governance and Nominating Committee

SHAREHOLDER INFORMATION

CALL-NET ENTERPRISES INC.

Head Office
2235 Sheppard Avenue East
Atria II, Suite 1800
North York, Ontario
M2J 5G1

Transfer Agent and Registrar
Call-Net's transfer agent and registrar is The R-M Trust Company, Toronto, Montreal and Vancouver. Changes of address or inquiries about shares and dividends should be directed to the transfer agent.

Stock Exchange Listings
The Common Shares of Call-Net Enterprises Inc. are listed on the Montreal and Toronto stock exchanges under the stock symbol CN. The Class B Non-Voting Shares of Call-Net are listed on the Montreal and Toronto stock exchanges under the symbol CN.B, and on Nasdaq under the symbol CNEBF.

Annual Meeting
The annual meeting of shareholders will be held at 11:00 a.m. on Wednesday, May 14, 1997, at The Royal York Hotel in Toronto, Ontario.

Shareholder Inquiries
Shareholder inquiries should be directed to: Office of the Vice President and Chief Financial Officer, at (416) 718-6457

Ownership and Voting Rights of Call-Net Enterprises Inc.
Call-Net Enterprises Inc. is a Canadian company widely held by public shareholders. Through its wholly-owned subsidiary, Sprint Canada Inc., the Company offers long distance telecommunications services to the public. As of February 28, 1997, the Company's shareholders' equity consisted of issued and outstanding Common Shares, Class B Non-Voting Shares and Class C Non-Voting Shares.

To ensure that the Company or its affiliates remain qualified to operate as a telecommunications common carrier pursuant to the Telecommunications Act (Canada), and the regulations made thereunder ("Telecommunictions Legislation"), the Articles of the Company impose certain restrictions on the issue and transfer of Common Shares of the Company to non-Canadians, as defined in the Telecommunications Legislation. The Board of Directors of the Company may establish, amend or repeal any procedure required to administer such restrictions on the issuance and transfer of the Common Shares of the Company.

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CALL-NET ENTERPRISES INC.

LOOKING

FORWARD TO

OUR SECOND

DECADE